

# IFRS in Brief

August 2007, **Issue 38**

This issue of IFRS in Brief covers the July 2007 meeting of the International Accounting Standards Board (IASB).

- discussing the joint venture project
- discussing the income taxes project
- discussing the earnings per share project.

In addition, at its July 2007 meeting the Board:

- discussed IAS 27 *Consolidated and Separate Financial Statements*
- considered topics for its annual improvements ED
- discussed recent International Financial Reporting Interpretations Committee (IFRIC) activities.

## Summary

At its July 2007 meeting the Board continued:

- discussing the post-employment benefits project
- discussing the conceptual framework project
- discussing the Exposure Draft (ED) of *Financial Instruments Puttable at Fair Value and Obligations Arising on Liquidation*
- redeliberating proposals in the ED of *Proposed Amendments to IAS 37 Provisions, Contingent Liabilities and Contingent Assets and IAS 19 Employee Benefits*
- redeliberating the proposed amendments to IFRS 2 *Share-based Payment – Vesting Conditions and Cancellations*

## Post-employment Benefits

The Board continued discussing its forthcoming discussion paper on phase I of the post-employment benefits project:

- The Board considered the following definitions of benefit promises proposed by the staff:
  - a defined contribution (DC) promise would oblige the employer to pay specified contributions to a separate entity (a fund) with the obligation being extinguished upon such payment
  - a defined return (DR) promise would include a contribution requirement based on current salary, and a promised return on those contributions linked to a change in an asset or an index

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- all other benefit promises would be defined benefit (DB) promises. The Board noted that a DC promise is effectively the same as a DR promise except that the employer would not have an obligation for the promised return in a DC promise. The Board instructed the staff to consider if DC and DR promises could be included in a single category with DB promises considered as a residual category.
- The Board tentatively decided that when a plan provides alternative benefit promises, in particular, alternatives that offer the higher of two or more benefit promises (a “higher of promise”):
  - if one of the benefits is a DB promise, then it would be classified as a DB with a higher of promise
  - DB promise liabilities would be measured in accordance with IAS 19 *Employee Benefits*
  - higher of promise liabilities would be measured at fair value with changes in fair value disaggregated into service cost (i.e., the initial recognition of the liability) and fair value gain or loss (i.e., the amount arising from the subsequent remeasurement of the liability); changes in the fair value of such liabilities would be recognised in profit or loss.
- The Board tentatively decided that the accounting for plans with different benefit event alternatives (e.g., certain benefits provided if the employee reaches retirement and other benefits provided if the employee dies before retirement) would be outside the scope of phase I of the post-employment benefits project.
- In respect of splitting a DR promise into separate contribution and return requirements, the Board tentatively decided:
  - any deficit in a funded plan resulting from a reduction in the value of the assets to below

the respective contribution would be recognised in the return component (i.e., not the contribution component)

- a contribution requirement would be measured using the discounted specified unpaid contributions (i.e., does not include performance risk)
- a return requirement would be measured at fair value assuming there would be no change in past service benefits.
- In addition, the Board tentatively decided:
  - that unvested past service costs would be recognised when a plan amendment occurs
  - to include in the discussion paper different proposals on remeasurement presentations that separate gains and losses arising on remeasurement from other gains and losses.
- With respect to whether an employer should recognise an additional liability when the benefits owed to an employee who leaves immediately after the reporting date are more than the liability recognised at the reporting date, the Board tentatively decided to include a discussion of this issue in the discussion paper.

### Conceptual Framework

The Board discussed three phases of the conceptual framework project with one tentative conclusion reached:

- Elements and recognition (phase B)
  - the Board directed the staff to continue its focus on the working definition of an asset.
- Measurement (phase C) – the Board deliberated concepts of measurement, principles and terms.
- Reporting entity (phase D) – the Board tentatively decided to allow 120 days for comment on the forthcoming discussion paper / preliminary views document on this phase.

### Financial Instruments Puttable at Fair Value

The Board continued discussing responses to the ED *Financial Instruments Puttable at Fair Value and Obligations Arising on Liquidation*. The Board discussed but did not conclude on the level of participation in an entity’s performance that a puttable instrument must have in order to be considered an equity instrument.

### Provisions

The Board continued redeliberating proposals in the ED of *Proposed Amendments to IAS 37 and IAS 19* and tentatively affirmed that:

- a present obligation gives rise to a liability, and in particular:
  - a duty or responsibility to an external party results in an obligation
  - present obligations and future events exist independently
  - both a liability and a business risk may give rise to future outflows of economic benefits
- a stand ready obligation (i.e., uncertainty exists about the outflow of economic benefits required to settle a present obligation) is a liability
- indicators (e.g., past experience, similar items, additional evidence obtained after the reporting date) would be used as guidance in order to address uncertainty about the existence of a present obligation
- the difference between a constructive obligation and an obligation is that a constructive obligation is not legally enforceable and to emphasise in the final standard:
  - that a constructive obligation must involve a present obligation
  - that a management decision or intention to incur a future outflow of economic benefit does not necessarily give rise to a liability
  - the current definitions of legal and constructive obligations.

### Share-based Payment

The Board continued redeliberating existing divergences between IFRS 2 *Share-based Payment* and the U.S. standard SFAS 123(R) *Share-Based Payment* highlighted in the proposed amendment to IFRS 2 – *Vesting Conditions and Cancellations*.

Previously the Board decided to work towards a final amendment to IFRS 2 even with the potential grant date determination differences between IFRS 2 and SFAS 123(R). In this meeting however the Board discussed but did not conclude on whether clarifying the potential grant date determination difference should be included as part of the current amendment, or be completed as a separate project. The Board instructed the staff to prepare a paper on this item.

### Joint Ventures

The Board discussed the joint venture project and tentatively decided that an investment would not be remeasured at fair value when an investor retains significant influence, having lost joint control.

The Board also tentatively decided that the ED would draft an entirely new IFRS for joint arrangements (i.e., not a revision of IAS 31 *Interests in Joint Ventures*).

### Income Taxes

The Board discussed the proposed revision of IAS 12 *Income Taxes* and tentatively decided:

- the following definitions would apply:
  - a tax credit is a benefit granted by tax authorities that reduces tax payable
  - an investment tax credit is a tax credit directly related to acquiring a depreciable asset
- to reverse the following previous tentative decisions:
  - IAS 12 was to have included guidance on special deductions (i.e., IAS 12 would now stay silent on special deductions)
  - deferred tax assets and liabilities would have been measured using probability weighted average tax rates (i.e., IAS 12 would continue to use rates “expected” to apply)
- with regard to the effect of future distributions, when measuring current or deferred tax assets or liabilities, entities would use past practices and future expectations of distributions in jurisdictions:
  - that have a different tax rate for distributed and undistributed taxable earnings
  - that provide deductions for distributions to owners providing that the entity would have both the intention and the ability to make such distributions.

### Earnings per Share

The Board discussed the earnings per share project and tentatively decided with respect to the calculation of earnings per share (EPS):

- that the “fair value method” would be applied to instruments containing an embedded option accounted for at fair value through profit or loss
- actual dividends rather than hypothetical dividends would be used when applying the two-class method.

The Board also tentatively decided that the ED on the revised IAS 33 *Earnings per Share* would have a 120-day comment period.

### Consolidated and Separate Financial Statements

The Board discussed accounting for the formation of a new parent in separate financial statements and tentatively decided to amend IAS 27 to clarify that a reorganisation of an existing group (i.e., creating a new parent entity without any changes to the group in substance) would be accounted for using existing carrying amounts.

### Annual Improvements

The Board tentatively decided that annual improvements would be applied retrospectively unless impracticable and to allow early adoption of annual improvements, as long as all annual improvements are adopted together. The Board also confirmed a 90-day comment period for the forthcoming annual improvements ED.

As part of its forthcoming annual improvements ED the Board decided to propose amending:

- IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* to clarify that if an entity will lose control of a subsidiary as part of a committed sale plan, then it would classify such subsidiary’s assets and liabilities as held for sale
- IAS 36 *Impairment of Assets* to specify that when an entity uses fair value less costs to sell to estimate a recoverable amount, the entity would have the same detailed disclosure requirements that apply to value in use estimates of recoverable amounts
- IAS 17 *Leases* to remove guidance in relation to leases of land (IAS 17.14 and 15) that duplicates general guidance applying to all leases (IAS 17.8 – 12)
- IAS 10 *Events after the Balance Sheet Date* to clarify that dividends declared after the reporting date are not recognised as a liability because there is no present obligation
- IAS 19 *Employee Benefits* to clarify that return on plan assets would not include plan administration costs included in the defined benefit obligation actuarial assumptions
- IAS 23 (Revised) *Borrowing Costs* to improve consistency with IAS 39 *Financial Instruments: Recognition and Measurement* by referring to the use of the effective interest rate as a component of borrowing costs
- IAS 34 *Interim Financial Reporting* to improve consistency with IAS 33

by requiring only entities within the scope of IAS 33 to disclose earnings per share in interim financial statements.

#### **IFRIC Update**

The Board received an update on IFRIC activities, which included:

- publishing two tentative decisions in relation to IAS 39
- asking the Board to consider as part of its annual improvements process or other projects:
  - IAS 12 – the treatment of deferred taxes arising from unremitted foreign earnings

- IFRS 5 – how the remaining non-controlling equity investment would be measured after selling a controlling interest in a subsidiary
- IAS 18 *Revenue* – the need for additional guidance on identifying agency relationships
- IAS 39 – the ability to use purchased options to hedge future cash flows.

#### **IASB Observer Notes**

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